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relational contracts to assign rights and responsibilities to define compliance, a role that trade accords often confer on impartial third parties.[20]

Finally, legalistic dispute settlement also improves the expected value of reciprocal trade pacts through its impact on the behavior of private traders and investors. For political leaders to realize fully the benefits of liberalization, private sector actors must believe that having committed specific assets to production for (or sales in) foreign markets, they will not be denied access to that market. Traders and investors are risk-averse with respect to decisions about investment, production, and distribution involving assets that are highly specific – in other words, assets that are costly to convert to other uses.[21] Other things being equal, they prefer minimum uncertainty, prizing a stable policy environment in which to assess alternative business strategies.[22] Legalistic dispute settlement serves as an institutional commitment to trade liberalization that bolsters the confidence of the private sector, reducing one source of risk. The private sector thus increases the volume of trade and investment among the parties, amplifying the macroeconomic – and, in turn, political – benefits of liberalization.

* * *

Assessing the Trade-off

Political leaders negotiating the design of dispute settlement always confront this tension between policy discretion and treaty compliance. The trade-off between these objectives is universal, but not uniform. Different governments assess it in dissimilar ways. And the weight a specific government assigns to each objective changes in different settings, as does the probability that its preferred mechanism will be adopted. In specifying the dimensions of variance, it is helpful to distinguish two stages in the process of dispute settlement design. The first is national preference formation; the second, international bargaining.[23]

[20] See Garrett and Weingast 1993; and Weingast 1995.

[21] Not all assets, obviously, are specific. For a discussion, see Frieden 1991, 434–40, who builds on the pioneering work of Oliver Williamson. Williamson 1985.

[22] Not all firms prefer stable, liberal trade policy to the prospect of future protection. Firms close to insolvency or in sectors with low productivity are likely to prefer trade policy discretion – and the increased probability of protection – to legalistic dispute settlement.

[23] This distinction follows Moravcsik 1993, 480–82.

The level of legalism preferred by a particular government in a specific trade negotiation depends on several factors. The first is the extent to which its economy depends on trade with other signatories to the accord. The more trade-dependent the economy, measured as the ratio of intra-pact exports to gross domestic product (GDP), the more legalistic the dispute settlement mechanism its government will tend to favor. Legalistic dispute settlement is more valuable politically where trade with prospective partner countries accounts for a larger share of the domestic economy.

A second source of dispute settlement preferences is relative economic power. The more powerful the country in relative terms, the less legalistic the dispute settlement mechanism its government will favor. This hypothesis derives from the distinction between rule-oriented and power-oriented dispute settlement.[24] Rule-oriented systems resolve conflicts by developing and applying consistent rules to comparable disputes, enabling less powerful parties to win independent legal rulings that may be costly for more powerful parties to ignore. For small countries, the benefits of such rulings may outweigh the costs of diminished policy discretion. In power-oriented systems, parties resolve disputes through traditional diplomatic means of self-help, such as issue-linkage, hostage taking, and in particular the threat of retaliatory sanctions.[25] These strategies systematically favor more powerful countries, which tend to favor pragmatism over legalism. A telling measure of relative economic power within regional trade accords is each country's share of total pact GDP. The larger the country's economy in relative terms, the more influence it is likely to wield as the destination of imports from other signatories. Larger economies also tend to be less dependent on exports, giving their leaders diplomatic leverage in trade disputes.[26]

A third factor shaping dispute settlement preferences is the proposed depth of liberalization. Trade agreements come in a variety of forms, and the type of agreement at hand influences the type of dispute settlement system favored by member governments. In particular, the more ambitious the level of proposed integration, the more willing political leaders should be to endorse legalistic dispute settlement. One reason is that deeper integration promises to generate larger net economic gains.[27] A second

[24] For discussions of this distinction, which is also cast as "pragmatism" versus "legalism," see Dam 1970, 3–5; Hudec 1971, 1299–1300, 1304; and Jackson 1979.

[25] Yarbrough and Yarbrough 1986.

[26] Alesina and Wacziarg 1997.

[27] The same logic applies to the breadth of trade pacts: where coverage is comprehensive, excluding no major export sectors, political leaders are more likely to endorse legalism than in pacts that exempt significant sectors.

consideration is that legalism, viewed from a functional perspective, may be the most appropriate institutional design for the resolution of disputes in the process of deep integration, which includes coverage of complex nontariff barriers to trade and common regulatory regimes. *

Together these simple measures – intrapact trade dependence, relative economic power, and depth of liberalization – provide a way of specifying dispute settlement preferences *ex ante*. To specify outcomes, one must also identify which country's preferences – given divergent ideal points on the Pareto frontier of trade cooperation[28] – should prevail at the bargaining stage. Like most international treaty negotiations, trade talks require consensus. In the presence of a unanimity rule, the design of dispute settlement is likely to be only as legalistic as the signatory that most values policy discretion and least values treaty compliance will allow. The lowest common denominator drives the institutional outcome when all parties have a unit veto.

In trade negotiations, one proxy for legalism's lowest common denominator is intrapact economic asymmetry. Its utility lies in the fact that larger economies stand to gain less, in proportional terms, from regional liberalization than smaller economies. Within a given agreement, the largest economies – defined in terms of aggregate GDP – traditionally represent the most valuable potential markets for intrapact exports.[29] Larger economies also are less dependent on and less open to trade – with openness measured either in terms of policy measures or as the ratio of trade to GDP – than smaller economies.[30] [The] benefits of openness to trade, measured in terms of the impact on per capita GDP growth rates, diminish as aggregate GDP increases.[31] [Hence] the relative value of liberalization – and, by implication, of legalistic dispute settlement – is usually lower to larger economies than to smaller economies. The signatory state with the largest economy, therefore, is most likely to wield the unit veto that determines the level of legalism in a given agreement.

[28] Krasner 1991.

[29] For this observation to hold, per capita income levels should be comparable across member countries. Most regional trade pacts between 1957 and 1995 have been exclusively among either developed or developing countries, with NAFTA as the first of few exceptions.

[30] Alesina and Wacziarg report a strong negative correlation between country size and openness to trade. Alesina and Wacziarg 1997. This finding is robust across multiple measures of both variables, but of particular relevance to this study is their analysis of size based on the log of aggregate GDP.

[31] Alesina, Spolaore, and Wacziarg 1997.

This analysis leads one to expect less legalistic dispute settlement in accords between parties whose relative economic size and bargaining leverage are highly unequal. In pacts where a single member country is much larger than its partners – in other words, where intrapact economic asymmetry is high – the regional hegemon, whose economy stands to gain least from trade liberalization, has little incentive to risk its policy discretion on behalf of improved treaty compliance. Moreover, this hegemon also has the bargaining leverage to impose its preference for a pragmatic, power-oriented system, under which it can more effectively use unilateral trade measures. In other words, size matters – and significant disparities in relative economic position augur poorly for legalism. Legalistic dispute settlement is expected only in accords among parties whose relative size and bargaining leverage are more symmetric. In settings of low economic asymmetry – provided the proposed liberalization is sufficiently deep – all member governments have an incentive to improve treaty compliance through the use of impartial third parties. Given their comparable economic power *ex ante,* no signatory stands to lose bargaining leverage *ex post* from the transition to a legalistic system. The projected gains from liberalization must be significant, however, if political leaders are to compromise their policy discretion. If the level of integration is not ambitious – or if the pact exempts crucial export sectors – officials may very well reject legalism even in settings of low asymmetry.

* * *

THE DATA SET

Among advanced industrial and developing countries alike, regional trade integration has been a persistent feature of the world economy in recent decades. Counts vary, but no fewer than sixty regional trade arrangements, established through formal treaties, have come into being since 1957.[32] ***

Despite the general trend toward formal economic integration, these trade pacts differ on many dimensions[: size, members' level of economic development, the scope or depth of liberalization, levels of compliance, and durability.]

[32] In 1994 the International Monetary Fund compiled a list of more than sixty-eight regional agreements. An earlier study listed thirty-four existing and nineteen prospective arrangements. See IMF 1994; and de la Torre and Kelly 1992.

With such a diverse set of possible cases, it has been necessary to apply certain criteria to ensure comparability. In this study there are no restrictions on the number of signatories, though I do exclude GATT and the World Trade Organization – which stand alone as the world's only multilateral trade institutions ***. Similarly, there are no categorical restrictions on the type of agreement, with free trade areas, customs unions, common markets, and economic unions all represented. Finally, to minimize selection bias, the data set includes both successful and failed pacts. *** Despite these inclusive rules, trade agreements that failed to meet one or more of the following requirements did not qualify for this study.

First, liberalization must be reciprocal. Concessions need not be strictly equivalent or simultaneous. *** But at least among some core signatories, reciprocal market access must be the rule. ***

Second, liberalization must be relatively comprehensive in scope. Universal free trade, with no sectoral exceptions at all, is by no means required. Still, coverage of at least merchandise trade must in principle be broad. ***

Third, the trade pacts must have been signed between January 1957 and December 1995. Negotiations that did not produce specific liberalization commitments by the end of 1995 are excluded. Pacts in which implementation was at that point incomplete but in which liberalization had begun are incorporated. ***

Table 14.2 lists the sixty-two trade agreements that met these criteria. It also lists the year in which each treaty was signed and all member governments, identifying those governments that were not among the original signatories by indicating their years of accession in parentheses. Countries that signed but later withdrew from the agreement are noted, as are their years of departure. Appendix B lists the treaties from the relevant time period that failed to meet one of the first two criteria listed earlier, as well as those whose texts were for various reasons unavailable. As Table 14.2 suggests, one potential problem in the data set is a lack of independence among certain cases. There are four clusters of agreements, one in the Americas and three in Europe, within which the timing and terms of the accords are rather similar. So as not to exacerbate this problem, I exclude treaties that were later encompassed or superceded by subsequent agreements; examples include the Canada–U.S. Free Trade Agreement and various bilateral pacts between the EC and individual European Free Trade Association (EFTA) countries, almost all of which were replaced either by accession to the EC or by membership in the European Economic Area (EEA).

TABLE 14.2. *Data Set of Selected Regional Trade Agreements, 1957–95*

Pact	Year signed	Members[a]
AFTA (ASEAN Free Trade Area)	1992	Indonesia, Malaysia, Philippines, Singapore, Thailand, Brunei, Vietnam (1995), Laos (1997), Burma (1997)
Andean Pact	1969	Bolivia, Colombia, Ecuador, Peru, Venezuela (1973) (Chile withdrew in 1976)
ANZCERTA (Australia–New Zealand Closer Economic Relations Trade Agreement)	1983	Australia, New Zealand
Baltic Free Trade Agreement	1993	Estonia, Latvia, Lithuania
CACM (Central American Common Market)	1960	El Salvador, Guatemala, Honduras, Nicaragua, Costa Rica (1963) (Honduras withdrew in 1970 but rejoined in 1990)
CARICOM (Caribbean Community)	1973	Antigua and Bermuda, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname (1995), Trinidad and Tobago (Bahamas is a member of the Community but not of the Common Market)
CEAO (West African Economic Community) (dissolved in 1994)	1973	Benin, Burkina Faso, Ivory Coast, Mali, Mauritania, Niger, Senegal
CEEC (Central and East European Country) Pacts (5)		
Bulgaria–Czech Republic Free Trade Agreement	1995	Bulgaria, Czech Republic

(continued)

TABLE 14.2 *(continued)*

Pact	Year signed	Members[a]
Bulgaria–Slovak Republic Free Trade Agreement	1995	Bulgaria, Slovak Republic
Hungary–Slovenia Free Trade Agreement	1994	Hungary, Slovenia
Romania–Czech Republic Free Trade Agreement	1994	Romania, Czech Republic
Romania–Slovak Republic Free Trade Agreement	1994	Romania, Slovak Republic
CEFTA (Central European Free Trade Agreement)	1992	Czech Republic, Hungary, Poland, Slovakia, Slovenia (1996), Romania (1997)
Chile and Mexico Pacts (9)		
Chile–Bolivia Free Trade Agreement	1993	Chile, Bolivia
Chile–Canada Free Trade Agreement	1995	Chile, Canada
Chile–Colombia Free Trade Agreement	1993	Chile, Colombia
Chile–Ecuador Free Trade Agreement	1994	Chile, Ecuador
Chile–Venezuela Free Trade Agreement	1991	Chile, Venezuela
Mexico–Bolivia Free Trade Agreement	1994	Mexico, Bolivia
Mexico–Chile Free Trade Agreement	1991	Mexico, Chile
Mexico–Costa Rica Free Trade Agreement	1994	Mexico, Costa Rica
Group of Three Free Trade Agreement	1994	Colombia, Mexico, Venezuela

Pact	Year signed	Members[a]
CIS (Commonwealth of Independent States)	1993	Russia, Armenia, Azerbaijan, Armenia, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Tajikistan, Turkmenistan, Uzbekistan (Ukraine is a full member of the CIS but an associate member of the Economic Union)
COMESA (Common Market for Eastern and Southern Africa)	1993	Angola, Burundi, Comoros, Djibouti, Eritrea, Ethiopia, Kenya, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Rwanda, Somalia, Sudan, Swaziland, Tanzania, Uganda, Zaire (1994), Zambia, Zimbabwe (Seychelles signed the treaty but does not participate)
EAC (East African Community) (collapsed in 1977; dissolved in 1984)	1967	Kenya, Tanzania, Uganda
EC (European Community)	1957	Austria (1995), Belgium, Denmark (1973), Finland (1995), France, Germany, Greece (1981), Ireland (1973), Italy, Luxembourg, Netherlands, Portugal (1986), Spain (1986), Sweden (1995), United Kingdom (1973)
EC Associations (12)		
EC–Bulgaria Association Agreement	1993	EC, Bulgaria
EC–Cyprus Association Agreement	1972	EC, Cyprus
EC–Czech Republic Association Agreement	1991	EC, Czech Republic

(continued)

TABLE 14.2 *(continued)*

Pact	Year signed	Members[a]
EC–Estonia Free Trade Agreement	1994	EC, Estonia
EC–Hungary Association Agreement	1991	EC, Hungary
EC–Poland Association Agreement	1991	EC, Poland
EC–Romania Association Agreement	1993	EC, Romania
EC–Slovak Republic Association Agreement	1991	EC, Slovak Republic
EC–Turkey Customs Union	1963	EC, Turkey
EC–Latvia Free Trade Agreement	1994	EC, Latvia
EC–Lithuania Free Trade Agreement	1994	EC, Lithuania
EC–Malta Association Agreement	1970	EC, Malta
EC–Israel Free Trade Agreement	1995	EC, Israel
ECOWAS (Economic Community of West African States) (revised in 1993)	1975	Benin, Burkina Faso, Cape Verde, Gambia, Ghana, Guinea, Guinea-Bissau, Ivory Coast, Liberia, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone, Togo
EEA (European Economic Area)	1992	EC, Iceland, Liechtenstein, Norway (Swiss voters rejected the EEA in 1992; Austria, Finland, and Sweden joined EC in 1995)
EFTA (European Free Trade Association)	1960	Iceland (1970), Liechtenstein (1991), Norway, Switzerland (United Kingdom and Denmark withdrew in 1973; Portugal in 1986; Austria, Finland (1986), and Sweden in 1994)

Pact	Year signed	Members[a]
EFTA Agreements (12)		
EFTA–Bulgaria Agreement	1993	EFTA, Bulgaria
EFTA–Czech Republic Agreement	1992	EFTA, Czech Republic
EFTA–Estonia Agreement	1995	EFTA, Estonia
EFTA–Hungary Agreement	1993	EFTA, Hungary
EFTA–Israel Agreement	1992	EFTA, Israel
EFTA–Latvia Agreement	1995	EFTA, Latvia
EFTA–Lithuania Agreement	1995	EFTA, Lithuania
EFTA–Poland Agreement	1992	EFTA, Poland
EFTA–Romania Agreement	1992	EFTA, Romania
EFTA–Slovak Republic Agreement	1992	EFTA, Slovak Republic
EFTA–Slovenia Agreement	1995	EFTA, Slovenia
EFTA–Turkey Agreement	1991	EFTA, Turkey
GCC (Gulf Cooperation Council)	1981	Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates
Mano River Union	1973	Liberia, Sierra Leone, Guinea (joined after 1974)
MERCOSUR (Common Market of the South)	1991	Argentina, Brazil, Paraguay, Uruguay (Chile and Bolivia are associate members)
NAFTA (North American Free Trade Agreement)	1992	Canada, Mexico, United States

(continued)

TABLE 14.2 *(continued)*

Pact	Year signed	Members[a]
OECS (Organization of East Caribbean States)	1981	Antigua and Bermuda, Dominica, Grenada, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines
SACU (Southern African Customs Union)	1969	Botswana, Lesotho, Namibia, South Africa, Swaziland
U.S.–Israel Free Trade Agreement	1985	Israel, United States
UDEAC (Central African Customs and Economic Union)	1964	Cameroon, Central African Republic, Chad, Republic of Congo, Gabon, Equatorial Guinea

[a] Dates in parentheses indicate years of accession for member states that were not among the original signatories. Countries that signed but later withdrew from the agreement are also noted, as are their years of departure.

OVERVIEW OF REGIONAL DISPUTE SETTLEMENT

In this segment I summarize the level of legalism in each of the regional trade pacts in the data set. The basic features of dispute settlement in each pact are highlighted in Table 14.3, which draws on the treaty texts listed in Appendix A. Related agreements in Europe and the Americas are aggregated; within each group, dispute settlement provisions are identical in every important respect. I include two observations for EFTA, whose membership changed significantly over time (see Table 14.2) and whose 1960 dispute settlement system was transformed with the creation of the EEA in 1992. *** In this respect, EFTA is an exception to the rule. There are a handful of other agreements whose dispute settlement procedures changed over time – namely the Andean Pact, Central American Common Market (CACM), Common Market of the South (MERCOSUR), AFTA, and a few bilateral EFTA agreements. Unlike EFTA, however, these cases have not undergone radical changes in membership or in other variables of interest to this study. As a result, I report and evaluate their most recent dispute settlement design (citations for the relevant agreements are listed in Appendix A).

Table 14.3 underscores the dramatic extent of institutional variation in the data set. Its final column organizes the agreements into five clusters